FILED
OCT 13 1954
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1954

No. 330

ROY O. SHAFFER, Trustee, *Petitioner*

v.

THE UNITED STATES, *Respondent*

On Petition for a Writ of Certiorari to the United States Court of Claims

REPLY BRIEF FOR THE PETITIONER

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1. The most notable feature of the brief in opposition is its studied silence concerning the lower court's unprecedented pronouncement that the Government exercises a lawful prerogative in "demanding a change" in a public contractor's management (R. 126, App. 34), even where there is no contractual provision of a satisfactory management clause (Pet., p. 15). No effort is made to defend or explain the propriety of this startling principle—subjecting the affairs of private business enterprises to government control—notwithstanding its far-reaching future

impact upon the legal relations between the United States and its contractors.

Instead, this Court is asked to permit this radically new doctrine to take effect without review on two grounds, both of which are demonstrably untrue on the face of the findings below and under elementary decisional law. It is first intimated—but, significantly, not expressly stated—that the facts are in dispute (Opp., p. 3). This is the basis for a plea that the Court should deny certiorari because it will otherwise be faced with the burdensome task of examining "the complex facts of this case" (Opp., p. 21). It is further asserted that "even if any of Petitioner's substantive contentions are correct, he has shown no damages" (Opp., p. 20). Neither premise is defensible.

2. The truth is that the facts are not in dispute. This, indeed, is evidenced by the Government's failure to back up, with even a single illustration, its grave charge that the Petition "make[s] statements which purport to be but are not facts" (Opp., p. 3). What the Government seeks to do is create the impression of a factual dispute where none exists, by misrepresenting the findings below and omitting reference to all embarrassing facts. Compare, for example, the Government's version with the findings below as to the facts which caused Plaintiff to submit to the ouster of its management when confronted by O'Neill, the Surety representative, with the Navy's letter demanding the change. The Government says (Opp., p. 15):

> "The change in management which followed was not compelled by the Navy; it resulted rather from the desire of the surety and the bankrupt to create conditions such that additional funds from the Navy would be forthcoming and default by the bankrupt on the supply contracts would thereby be avoided."

Here is what the lower court said in its only finding of fact on the same subject (Fdg. 61, R. 177):

> "O'Neill went to Fort Worth promptly after receipt of this letter to discuss with plaintiff's officers

> and stockholders the situation which the letter created. The initial reaction of these people was to 'abandon' all of their Navy contracts, recognizing that plaintiff might incur a loss of $400,000 to $750,000 in the process. However, the surety company representative stated that he could not agree with this procedure, and that if plaintiff persisted in this position, the surety company would be forced to exercise the powers conferred upon it by the escrow agreements, *in effect taking control of plaintiff and of Texas Steel Company.* In the course of the subsequent discussions, the proposal was evolved that control of all operations at Port Arthur be put in the hands of a Management Committee. *This proposal was accepted by plaintiff's officers and stockholders, to avoid the possibility that Seaboard [the Surety] would take over these two businesses . . .*" (Emphasis supplied).

As the quoted findings are clear, Plaintiff's stockholder-managers were motivated to yield control of Plaintiff's Port Arthur plant because they were otherwise faced with the loss of their entire business, including their other organization, the Texas Steel Company, and also Plaintiff's profitable Fort Worth plant (R. 113, App. 22). Contrary to Respondent's present claim, the choice was thus impelled by economic duress, not by avarice for additional Navy funds.

No less misleading is the Government's following assertion (Opp., p. 16):

> "Moreover the changes were worked out by the surety and the bankrupt. The Navy took no part in the discussions that led to the appointment of the management committee and it did not appoint or suggest the appointment of anyone to the Committee."

But nowhere in its brief does the Government mention any of the succeeding facts, although it denies none of them:

(a) that early in April 1942, the Navy had procured an agreement that the Surety "would exercise its powers under the pledge-escrow agreement in ac-

cordance with the Bureau's wishes" (Fdg. 46, R. 166);

(b) that in a meeting of June 2, 1942, which is described in full at pages 10-11 of our Petition, the Chief of Ordnance ordered the Surety to use the pledge agreement to evict plaintiff's management—answering the Surety's objections that it had no right to do so and that Plaintiff's management was competent, with the dictate to "Go down there and chop their heads off";

(c) that because of "foreseeable legal objections," the Surety insisted upon the deletion of any reference to the pledge agreement, from the Navy's original letter demanding the eviction of Plaintiff's management from the Port Arthur plant and the vesting of performance of the facility and supply contracts in a three-man board on which Plaintiff would have only one representative (App. 29-30; Fdgs. 59-60, R. 175-177);

(d) that the Navy at all times retained the right to appoint a third member of, and the power to veto any changes in, the Management Committee (Fdg. 61, R. 177)—on which Plaintiff was limited to one representative, along with the Surety, just as specified in the Navy's letter to the Surety of June 5, 1942 (App. 30-31; Fdg. 59, R. 176).

These were the facts which forced the lower court to the necessity of ruling that the Navy had a right to demand a change in Plaintiff's management. They are totally incompatible with the present claims that there was no "taking" because the "operation of the management committee was voluntarily arranged by the surety and the bankrupt" (Opp., p. 13) ,and that there was no breach of contract because "the change in management was not the Navy's act but was brought about by the Surety to protect its own interests" (Opp., pp. 19-20).

There is not a line in the opinion or findings of fact below which even intimates that the Surety at any time expressed dissatisfaction with Plaintiff's management or had any part in initiating the ouster or had voluntarily ac-

quiesced in it. The undenied facts establish the contrary: that the Surety had expressed its confidence in Plaintiff's management; had tangibly manifested it by the issuance of its several bonds, amounting to $1,434,735.60 (Opp., p. 16); and had resisted as far as it could the Navy's order to evict Plaintiff's management (see Pet., pp. 10-11). When the Navy overrode its objections, the Surety had no alternative but to comply. The crucial fact was that the Navy, since early April 1942, had held the Surety's commitment to exercise its voting rights under the pledge-escrow agreement "in accordance with the Bureau's wishes" (Fdg. 46, R. 166). Breach of this commitment would have exposed the Surety to reprisal by the Navy, which held its bonds.

In short, the Surety was not a free agent. For, in substance and effect, the Navy held a proxy from the Surety to vote Plaintiff's stock. That proxy was exercised by the Chief of Ordnance in June 1942, when he told the Surety to exercise the pledge agreement to "go down there and get rid of them" (Pet., p. 11). In this situation, having conveyed instructions to its voting agent, (i.e., the Surety), the Navy had no need to participate directly in discussions with Plaintiff. That this was the whole and simple truth of the matter is shown by the Surety's response when Plaintiff's management declined to abdicate in order to obtain the additional funds, preferring instead to abandon the Navy contracts and absorb the concomitant losses. At that point the Surety, notwithstanding its recognition of the "legal objections" to the use of the pledge agreement (App. 29-30; Fdg. 60, R. 176), nevertheless threatened to invoke it, just as the Navy had directed, and thereby accomplished the change demanded by the Navy (Fdg. 61, R. 177-178).

The same circumstances also obviated any need for the Navy to exercise its reserved right to appoint a third member to the Committee. The Surety sat on the two-man Committee and not only did the Navy still retain the Surety's proxy, but it had affirmatively evinced its intention

to continue to use it. In its letters of June 5 and 6, 1942, demanding the change, it had instructed the Surety to make "periodic reports of progress" and to "retain a position where you can change management" (Fdgs. 59, 60, R. 176-7). And the conduct of both the Navy and Surety following the change further confirm their understanding that control of the Port Arthur operation thereafter remained in the Navy. On June 16, 1942, the Surety advised the Navy that the ouster had been effected "in order to comply with the wishes expressed in your letter of June 6th" and the Navy answered that the new arrangement "would be considered satisfactory until proved otherwise by experience" (Fdg. 62, R. 178; Defense Exhibit 89, p. 2).

Every single one of the above-stated facts was recited in the Statement of the Case set out at pages 4-13 of our Petition. Not a single one of them is controverted, or even mentioned, in the Government's Brief in Opposition. Those facts not only demolish the protestations that the Navy took no part in the removal of Plaintiff's management, but prove that the Navy alone forced the change and thereafter maintained control of the management. It follows that the United States is liable for a taking of Plaintiff's property (*United States* v. *General Motors Corp.*, 323 U.S. 373, 378) and also for breach of its contracts because of "an exercise of superintendance and unwarrantable superintendance . . . [which] . . . was an improper interference" (*United States* v. *Barlow*, 184 U.S. 123, 137).

3. We turn now to the Government's argument that no compensable damages were shown. The Court will note that this claim is not supported by any finding of fact or ruling of law below. Its lack of substance appears both from the record and the applicable legal authorities.

At pages 20 and 21 of the Brief in Opposition, the Government says that Petitioner's proof did not satisfy the asserted holding of *United States* v. *Pewee Coal Co.*, 341

U. S. 114, at 121, that the owner must show that the operating losses would not have occurred in the absence of the taking. But even under this view of the case, the findings below disclose that Petitioner met this burden. The contracts on which the losses were suffered called for the manufacture of shells. The following are the lower court's own words (App. 22; R. 113), supported by its Finding No. 2 (R. 127), concerning the results achieved by Plaintiff at its Fort Worth plant under the very management which the Navy evicted from the Port Arthur facility:

> "The plaintiff's corporate stock was owned entirely by members of the Armstrong family. In 1940 it made a contract with the War Department to manufacture shells at the plaintiff's plant in Fort Worth, Texas. From that time until the end of the war it produced shells at that plant efficiently, and at a large profit to itself."

There is the proof that Plaintiff knew how to operate a shell plant profitably. Plaintiff's management had nothing to do with the operating losses sustained at Port Arthur. The management was admittedly forced out before the plant was completed and before performance of the Navy shell contracts began (Opp., pp. 9-10).

The profit at Forth Worth amounted to $1,087,881.57 during the 1942-1944 period preceding the bankruptcy (Tr. 27-11) and constituted money belonging to Plaintiff. That money is part of what was taken from Plaintiff by the Navy's ouster of its management from the Port Arthur facility. The operating losses incurred under the Navy-imposed management at Port Arthur during the very same 1942-1944 period exhausted the entire Fort Worth profits and ran the Company into bankruptcy.

There is no merit in the effort to deny recovery to Plaintiff by asserting that "the settled rule is that the damages are the difference between what the bankrupt would have earned if the Government had performed the contracts

and what it actually earned" (Opp., p. 21). That, of course, is one measure of damages, but not the only one, particularly where the breach consists of interference whereby performance is prevented. *United States* v. *Smith*, 94 U. S. 214; *Parish* v. *United States*, 100 U. S. 500, 506-7; *United States* v. *Barlow*, 184 U. S. 123. "Where a breach of a contract interferes with the proper performance of a contract in accordance with its terms, the injured party may recover damages to the extent at least of any loss which was the necessary consequence of such interference. . . . The fact that he might recover more by way of lost profits, if proven, is not fatal" (*Needles* v. *United States*, 101 Ct. Cl. 515, 619).[1] On this record the operating losses suffered at Port Arthur plainly resulted from the Navy's interference with Plaintiff's management. They were incurred by the Navy-imposed Committee which took over the Port Arthur operation before the facility was completed and before performance of the supply contracts began (Opp., p. 10). In contrast to the Committee's huge losses on the Navy shell contracts at Port Arthur, the evicted management during the same period produced shells for the Army at its Fort Worth plant, "efficiently and at a large profit to itself" (R. 113, App. 22; Fdg. 2, R. 127).

In short, Respondent's argument that Petitioner is entitled to no damages for breach of contract rests on the novel proposition that he should be penalized for his restraint in seeking to have the contractor made whole for its out-of-pocket losses, without reference to lost profits.

4. The remainder of the opposing brief is similarly characterized by omissions of fact and mistakes of law. Respondent concedes, as it must, that "the surety company's right to take control of the bankrupt was contingent upon

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[1] The Court there rejected an identical argument to that made here, relying on this Court's holdings in the *Smith*, *Parish* and *Barlow* cases, *supra*. See 101 Ct. Cls. at 618-619.

the necessity of obviating a declaration of default by the Navy" (Opp., p. 15). The default cannot be spelled out of the facilities contract which called only for Plaintiff's "best efforts" to meet the Government's estimates (Fdg. 27, R. 150). Consequently, recourse must be had to the supply contracts. But here the Government is confronted by the express recital in the facilities contract that the supply contracts had been or were being entered into "on the understanding that the facilities for the same will be provided by the Department" (Opp., p. 17). It is therefore pressed to the curious and unsupported argument that the Navy did not mean what it said—that this was "merely a formal recital in standard phraseology of the Navy's justification for invoking the statutory authorization. It was not a part of the promises of the parties" (Opp., p. 18).

The argument not only ignores this Court's admonition that it will not "revise the contract which [the Government] draws on the ground that a more prudent one might have been made" (*United States* v. *Standard Rice Company*, 323 U. S. 106, 111), but is also opposed to the facts found below, which establish that the recital precisely and accurately reflected the actual understanding of the parties. The facilities contract in which the recital appears was executed October 14, 1941, following the execution of change orders, on October 4, 1941, reducing the original contract prices in express consideration of the Government's undertaking to provide the required plant (Fdg. 28, R. 153-154). A memorandum of the Chief of Ordnance to the Secretary of the Navy, dated October 6, 1941, recommending the provision of the facility, not only referred to the price reduction to be received in return, but expressly stated as follows (Fdg. 27, R. 148):

> "If the proposed expansion is not made, Contractor will be unable to deliver."

Later, on May 22, 1942, the Production Division of the Bureau of Ordnance, requested the required funds to com-

plete the facility, by a memorandum which stated in part (Fdg. 56, R. 174):

> "If we do not provide the facilities the surety company will probably be able to reduce or eliminate their responsibility under the Supply Contract because we did not supply the facilities, thereby making it impossible for the Contractor to carry out the Supply Contract."

. In short, the foregoing facts, ignored by Respondent, are clear that the Navy contemporaneously recognized that its provision of a facility was a condition precedent to Plaintiff's obligations under the supply contracts as amended by the change orders. The prerequisite default situation for invoking the pledge agreement was thus lacking, as the Surety itself recognized when it insisted upon the deletion of any reference to that agreement from the Navy's letters of June 5 and 6, 1942, demanding the removal of Plaintiff's management (App. 29-30; Fdgs. 59, 60, R. 176-7).

5. We do not quarrel with the Government's statement that it "is elementary that one who offers to advance money may lay down the conditions on which such money will be advanced" (Opp., p. 14). Of course it is. But the offeree is entitled to the prerogative to reject the offer and the facts are plain that the Navy had no thought or purpose of permitting the exercise of any such prerogative by Plaintiff. Otherwise, it would have made the offer directly to Plaintiff, instead of proceeding behind its back to force the Surety to get rid of the management by recourse to the pledge agreement.

6. The Brief in Opposition seeks to forestall a writ of certiorari by an effort to submerge the outstandingly important question decided below in a contrived and spurious factual dispute. That question concerns the extent of the Government's inherent authority to control the management of public contractors and has never been considered by this Court. The material facts are neither truly in dis-

pute nor complex. Petitioner's prayer for the writ is made in reliance upon the face of the lower Court's opinion and its findings of fact. The petition should be granted and the decision below reversed.

Respectfully submitted,

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